

CALIFORNIA FRANCHISE TAX BOARD

Legal Ruling No. 095

June 25, 1958

NONRESIDENT: SOURCE OF INCOME PAYMENTS

Syllabus:

Payments to a nonresident are held to be interest and therefore not income from California sources, even though based on oil royalty income.

Prior to 1940, taxpayer, a nonresident, loaned money to her son to purchase a ranch in California and took a mortgage on the property. In 1940 the son was having financial difficulties and taxpayer agreed to reduce the indebtedness. In consideration for the reduction the son agreed to that if oil was discovered on the mortgaged property, he would pay taxpayer one-fourth of the oil royalty income from the property until a stipulated amount was paid. This was in addition to the reduced balance of the indebtedness. Subsequently oil was discovered and one-fourth of the yearly oil royalties were paid to taxpayer until the stipulated sum was paid. Advice is requested whether the income paid to taxpayer, a nonresident, was taxable to her in California.

Taxpayer reported the payments as interest, not as royalties, in her federal returns and did not take depletion deductions. Taxpayer reported the payments in lieu of interest on the money she loaned her son, i.e., as consideration for reducing the balance of principal and interest due her. Viewed as interest, these payments are intangible in nature and not income from California sources. Consequently, taxpayer, a nonresident, is not liable for California income tax on the payments.